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CIA No. 7873
20 November 1973

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MEMORANDUM FOR: John Bushnell
National Security Council
Program Analysis
Room 481
OEOB 20506

SUBJECT : The Rice Situation in Southeast Asia

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The attached is a first draft of a report on Southeast Asian rice problems. It represents inputs from a number of country analysts and a steady research effort from the drafter of the Indonesian project we sent you earlier. We are considering publishing this piece and would appreciate guidance and comments from you on it by 28 November if possible.

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Attachment

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Regional Conclusions

Southeast Asia is seized with some of its most difficult rice supply problems since World War II. Following a poor crop in 1972/73, import demands for the region soared above normal levels, and this -- combined with global shortages of other grains -- contributed to a tripling of world rice prices. Although rice now available in the US and from Thailand should preclude a sharp decline in regional living standards, serious pressures experienced over the course of this year will have significant -- and, in some instances, longlasting -- adverse effects on the Southeast Asian economies.

Because rice is far and away the most important element of the diet throughout the region, skyrocketing rice prices will have a strong inflationary impact on all the countries of the region. Coming on top of other global commodity shortages and a paucity of natural resources throughout the region, the price increases in rice will create unusual and -- in some cases -- persistent stabilization problems. Moreover, with current world rice prices on the order of \$600 a ton, simply meeting food needs through imports may sharply reduce the scarce foreign exchange of the importing countries.

Despite the fact that this year's shortfalls could not have been adequately anticipated, Southeast Asian governments

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efficiency both to explain why better provisions were not made and to justify much more extensive government intervention in rice marketing. Generalized rice riots are unlikely, but the possibility of local disturbances will persist into 1974, and individual political fortunes may rise and fall with local rice availabilities.

For the long term, the major consequences of this year's shortfalls will likely be: 1) lingering government controls that tend to slow production growth; and 2) concerted efforts to rebuild depleted national inventories. These pressures will doubtless tend to keep prices up above pre-1973 levels and sustain a demand for continued large-scale US exports.

Discussion

1. Introduction

Southeast Asia is the world's largest market for international rice sales. World production of milled rice annually amounts to about 200 million tons, but most rice is consumed in the producing country, and only 3-4% enters world trade. Half of world imports, however, are accounted for by Southeast Asian nations. Rice is the dominant food in Southeast Asian diets, and annual consumption generally ranges from 100-150 kilograms per person. For the most part, ricefields constitute the bulk of cultivated area in the countries of the region, and rice accounts for over half of agricultural production. Despite this emphasis, however, Southeast Asia grows only one-fifth of the world's rice.

Against this background, this memorandum looks at the consequences for the countries of the region and key rice exporters of recent production shortfalls and a tight global rice market. Besides tracing the causes of national shortages, it considers what impact these will have on other aspects of the economy. Final sections briefly assess the trading prospects for the rest of this cropyear and next.

27. The Southeast Asian Rice Problem

Last year production declined in most of Southeast Asia as world output fell 5%. For the most part, the Southeast Asian declines were caused by poor weather. A long period of drought during the main 1972 crop season depressed Thai production. A lack of rainfall compounded by inappropriate government policies led to a one-sixth decline in Burma's rice output. In the Philippines, too much water was the case as disastrous floods in central Luzon, which supplies one-quarter of the Islands' rice crop, caused an almost 10% drop in production. This was the second major setback for the Philippines, as the previous year's crop was severely hit by disease. The Indonesia crop suffered from some pest damage and late rains, while South Vietnam and Cambodia experienced both weather and war-related declines.

Thus, at the beginning of the 1973/74 cropyear, Southeast Asian import demand was probably some 3.5-5.1 million tons, compared with 2.5-3.0 million tons for the previous year. This surge in demand has tripled world prices from about \$200 a ton in January to as much as \$600 a ton in October.* Moreover, world-wide wheat production setbacks and large international purchases by Russia and China have

* Prices for 1st grade, whole, white rice; FOB Bangkok

the strict controls on all grains, limiting the amount of substitution that could take place. As a result, many countries were forced to cope with decreased rice consumption, substitution of corn and other less-desirable starches for rice, and popular grumblings over governments' ability to handle the shortages. Indonesia, the world's largest rice importer, may double its rice import bill because of higher prices. Thailand -- which together with Burma has in the past supplied one-third to one-half of the rice entering world markets -- encountered a considerable drop in export availability earlier in the year, but should be able to compensate somewhat through judicious management of its export stocks. Burma, however, was hopelessly left behind, and had to consider the possibility of serious domestic shortages. Cambodia, a special case, has encountered critical rice supply difficulties throughout the year.

1. Burma

		Thousand Tons, Million
Rice Production (1973/74)	:	5,200 - 5,300
Rice Production (1972/73)	:	4,400
Exports (1973)	:	Less than 100
Exports (Average 1969-1972)	:	725

Lack of rainfall during the 1972/73 season was primarily responsible for production falling by 16% from the previous year, but several other factors were evident. There has been a general lack of government-sanctioned price incentives for producers to expand production beyond their own needs and whatever they might be able to sell in the free market. Prior to May 1973, the government maintained control over rice trade, and prices paid to farmers for paddy were too low to encourage a large surplus production. With rapidly rising prices for the goods farmers needed to buy, the resulting decline in real income militated against agricultural investment or improvement in production techniques. Instead, fertilization and irrigation

* All production and import figures are preliminary estimates or forecasts, and are subject to change as more information is available. Unless otherwise noted, single years denote calendar years; double years denote crop years generally running from July through June. Although there are recognized variations between countries, a milling rate of 65% is assumed.

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... and expensive, labor-intensive transplanting was replaced by low-cost broadcast seeding.

... incentives to sell for 350-500 higher prices on the free market, producers diverted from the government a portion of the surplus available for deficit areas and for export. Because of the government's failure to procure sufficient rice for deficit areas and for exports, the rice trade was decontrolled in May 1973, leaving private individuals free to buy, sell, transport, and process rice. Export trade remained a government monopoly, and the government continued to stock and sell rice for internal distribution to deficit areas. Although the decontrol measure elicited a cautious response from producers and traders, many of whom feared it was only temporary, it helped bring out some paddy hoarded by farmers, and also allowed cooperatives in rice-deficit areas to buy in surplus areas, albeit at high prices.

It was soon decided, however, that the response from producers and traders was not sufficient. In October, the government announced higher paddy prices, but also fixed quotas requiring farmers, after certain deductions, to sell 60% of their paddy to the government. Moreover, the way was cleared for strict enforcement of the quota requirement by authorizing personal property seizures, including confiscation of farmlands, in actions against farmers indebted to the government through agricultural loans. Although the new policy is slightly

...and violent reaction, especially if the currently
...government and open market prices
...
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The target for the 1973/74 crop, most of which is harvested in November and December of this year, is 8.2 million tons of paddy (about 5.3 million tons milled). Preliminary forecasts suggest that if the weather holds, this target should be reached. Planned exports for 1974 range from 700,000-900,000 tons, but 500,000-600,000 tons may be more likely because of procurement difficulties.

Over the longer term, there is little incentive for farmers to expand production much beyond subsistence needs. A chronic dearth of consumer goods and the lack of an organized, freely accessible market system result in little motivation to raise income levels through increased rice production. Insecurity in many areas further reduces incentives. Recent trends indicating that consumption increases outpace production increases by some 1.2% annually suggest a discouraging outlook for rice exports until these deep-seated difficulties are resolved.

Burma's acute rice shortage this year has had a considerable impact on the economy. Already-high rice prices began to edge upward in July. By mid-August, first-quality rice was being sold in Rangoon for the equivalent of \$0.57 a kilogram, compared

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... two months prior and about \$0.22 - \$0.26 in ...
... in upcountry and highland areas are ...
... -- almost \$2.00 a kilogram -- and shortages there ...
... that consumers have reportedly turned to corn, beans, and even roots for subsistence. Violence has apparently been avoided thus far and the situation should soften with the harvest now taking place. With the new procurement policy, however, the government may be buying peace with consumers at the cost of serious producer reaction.

The lack of rice for export will severely affect Burma's foreign exchange reserves this year. Burma runs a chronic current account deficit of \$50-\$60 million annually. Large capital inflows have helped to forestall rapid decline in gross reserves, which at the end of 1972 were some \$62 million -- equivalent to about four months of imports. Net reserves, however, were zero at the end of 1972. Total exports this year are likely to be less than \$80 million because of the lack of rice, compared with some \$120 million in previous years. Assuming a normal level of imports of some \$160 million, a trade deficit on the order of \$80 million for 1973 could be expected, over twice that of last year. Burma almost certainly had to cut back on imports this year, however, because of its poor reserve position and the unlikelihood of again enjoying large capital inflows -- on the order of \$60 million in 1972.

		<u>THOUSAND TONS. MILLION</u>
Rice Production (1973)	:	8,800 - 9,100
Rice Production (1972)	:	7,000
Exports (as of Sept 1973)	:	700
Exports (average, 1969-1972)	:	1,400

Preliminary estimates suggest that the 1973 crop will be substantially larger than the drought-stricken 1972 crop, and may be as much as 13.5-14.0 million tons of paddy. Weather conditions have been generally good. Some flooding of the summer crop was reported, but it is not known if damage was sufficient to radically change the optimistic harvest estimate of 500,000-550,000 tons of paddy. The main fall crop reportedly looks very good so far, and should be about 13 million tons of paddy.*

Rice exports have suffered from the poor harvest last year. Thailand exported over 2 million tons of rice in 1972, almost 30% of the rice traded in the world market. This year, however, only some 682,000 tons had been exported as of September. Because of the crop shortfall and the need to insure domestic requirements first, Bangkok banned exports at midyear, except for small purchases by several Asian nations. It was not until September, after the arrival of ~~the~~ including an early-fall crop of some 500,000 tons.

... crop, that the first large export of 52,000 tons to Hong Kong, Singapore, and the Middle East was authorized.

High market prices and continued high export demand point to high returns to producers from expanded production. Thai growers, however, have not been particularly successful in making quick production adjustments. Most increases have taken place by expanding the planted area, but on ever poorer lands. Rice yields are less than two tons per hectare, substantially less than Indonesia, Taiwan, South Vietnam, or Korea, for example. The new high-yield rice varieties account for only 23 of plantings, the lowest in any Asian country. Fertilizer applications are especially low, largely because of high fertilizer costs, but also because there has been little incentive -- up until now -- to produce an even greater rice surplus.

Despite continuance of its surplus, Thailand's position in the global shortage has not been a complete blessing. Domestic rice prices have risen sharply at farm, wholesale, and retail levels, and this has impacted on consumer prices in general. Although domestic markets are partly insulated from world markets by a rice premium and other taxes and regulations,* wholesale and paddy prices at midyear were nearly double levels a year earlier. For the first seven months of 1973, the wholesale

*The rice premium is a tax paid by exporters, to the government, to equalize Thai export prices with world prices; regulations include, for example, requiring exporters to set aside for domestic sale a specified quantity of rice for each ton exported.

... other world gains for a country used to loss
... its currency in June.

Nevertheless, nothing in the recent global rice shortages
... serious short-term economic problems for Thailand.
The potentially good harvest expected this year will insure
adequate supplies of foodstuffs over 1974. Moreover, foreign
exchange reserves of \$1.1 billion at the end of September --
equivalent to 9 months of imports at the 1972 level -- also
provide a comfortable cushion for alleviating pressures on
prices through increased imports of other consumer goods.

A more serious danger for the other countries of the
region is that the new Thai government will feel a need for
the maximum possible insurance against both rice shortages
and sudden price increases and will choose to turn the flow
of rice exports on and off accordingly. Some precedent for
this already exists in the earlier export ban, and the difficult
bargaining Cambodia has faced in its efforts to secure much-
needed supplies tends to reinforce this impression.

As smaller amounts of rice have been exported, Thailand
has passed up the opportunity to reap the fullest benefit
to its own growth from high global prices. Last year, foreign
exchange earnings from rice amounted to \$200 million, 20% of
total merchandise earnings and 12% of total exchange earnings.

... total export receipts from rice will likely run
... and order even though prices have tripled in the
... market.

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1. Cambodia

Thousand Tons, Milled

Rice Production (1973/74)	:	500
Rice Production (1972/73)	:	600
Import Requirements (Annual)	:	150-200

Rice production declined dramatically with war and the attendant disruption of transport and marketing systems and the exodus of over one million peasants from the countryside beginning in 1970. The fall was particularly rapid after 1971 as the government progressively lost control of traditional rice-surplus areas. Government economic policies, too, were partly to blame. Artificially low, controlled rice prices, established early in the war to avoid political repercussions of rising food costs, provided no incentive for farmers to continue or expand production in the face of difficult security and marketing conditions.

The difficulty in both obtaining rice for import on tight world markets and insuring the steady internal flow of rice over often-interdicted transport routes has generally prevented Phnom Penh**from amassing stocks sufficient for more than

* See Appendix A for separate discussion of North Vietnam's rice situation.

** Refugee-swollen Phnom Penh, with a population of some 1.5 million out of Cambodia's total of 7 million, is the major rice-deficit area under government control. With a few exceptions, other government areas are considered relatively self-sufficient; food conditions in enemy areas are indeterminate and not considered here.

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at a time. Despite pressures from the US, the government has been unwilling to significantly limit the distribution of rice from its warehouses to retail outlets, and the combination of increased refugee requirements and hoarding in anticipation of future shortages has seriously increased market pressures. This condition became critical in mid-October, when transport disruptions and difficulty in contracting for rice imports pushed capital-city stocks down to a 5-6 day level. The situation was particularly acute because imports through the US PL-480 program would not begin arriving until December.

Phnom Penh's crisis began to improve in late October with large-scale arrivals of rice from South Vietnam and Thailand. As of 28 October, government stocks were sufficient to cover two weeks' consumption. Scheduled deliveries from Thailand, South Vietnam, and South Korea should increase the capital's stocks to around two months' supply by the end of November. Negotiations to obtain additional rice from Japan (5,000 tons) and South Korea (11,200 tons) were recently successful, and shipments could reach Phnom Penh as early as December, concurrent with initial arrivals of US PL-480 and newly-harvested domestic rice. The timely arrival of imported rice is, however, still an issue of concern. Even if transport routes can be secured, the amount of rice available for the capital area from Cambodia's small domestic harvest will probably be sufficient for only several months.

Cambodia's current economic woes derive in no small measure from the deterioration in domestic rice supplies, and these in turn have added to political pressures. Rice shortages have been the principal cause of a 500% increase in the cost of living since the war began and the more than doubling of prices this year alone.* Freight charges on the PL-480 rice of about \$10 million in 1973 had to be financed by Cambodia's limited foreign exchange reserves at the expense of needed merchandise imports; the US will probably fund freight expenditures in 1974. Although there has been little public reaction to constantly rising rice prices, the potential for a complete drawdown of the city's stocks has several times engendered riots and destruction and looting of largely Chinese retail shops. The government has been generally successful in putting down these disturbances, not so much out of its own power but out of the failure of the spontaneous rice riots to develop into a mechanism for political upheaval; still, the potential is there.

Although Cambodia will continue to require substantial rice imports until peace is restored, its longer term prospects

* Rice accounts for over one-third of the price index, but with rice prices up some tenfold over the prewar level, the erosion of real incomes, and the high price and unavailability of other commodities, the index grossly understates the importance of rice in consumer expenditures.

Prior to 1970, Cambodia exported some 200,000 tons of rice annually. Population pressures are not great, and land is in good supply. Prewar production levels could be easily reached with the opening of transport and marketing systems and an appropriate program to return refugees to their lands. Little had ever been done in the line of irrigation and fertilization -- Cambodia's rice yields were among Asia's lowest -- and rapid gains could probably be achieved through the introduction of high-yield rice varieties and ancillary inputs.

~~CONFIDENTIAL~~Thousand Tons, Milled

Crop Year Begins 1 April)

Rice Production (1973/74) : 12,400

Rice Production (1972/73) : 12,200

Imports Required (1974) : 800

Rice production for the 1973/74 crop year should be slightly better than last year's but clearly less than the record 12.8-million-ton 1971/72 crop. The main crop, which is harvested from April through June and accounts for 70% of production, was probably smaller than in 1972 because of pest damage and late rains. The dry season crop, harvested from September through November, however, is expected to be better than last year's drought-stricken output.

Despite this rather hopeful crop picture and energetic import efforts, Indonesia faces stock and distribution problems resulting from the government's domestic rice procurement program. BULOG, the government purchasing agency, has been able to purchase only some 250,000 tons of rice, less than 20% of its admittedly unrealistic target of 1.5 million tons. BULOG's initial procurement efforts, based on a quota system, were ill-planned and oppressive, and severely disrupted the free market system. Many villagers

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Since the government had lost its credibility and would fail to react to local problems. Farmers reacted by withholding rice, and the amounts on markets accordingly shrank. In late August, Jakarta abandoned the quota system, permitted local requirements to be insured first, and established more consistent price regulations for government purchases. It is not yet known whether these measures have increased the flow of rice either into government or private channels.

With small official rice holdings, the government aggressively went into the world market to purchase enough rice: 1) for allocations to government employees and market stabilization; and 2) to supply deficit areas. Of total import needs, estimated by the Indonesians at about 1.9 million tons for the cropyear April 1973 to March 1974, 1.4 million tons had been contracted for by the end of August. The Indonesian estimate reflected maximum demand, however, including a stock buildup that is unlikely until world supplies increase considerably. Scheduled arrivals should meet domestic requirements at least through February 1974. Indonesia will still have to contract for substantial imports* -- on the

* Relatively high foreign exchange reserves -- \$852 million as of September, equivalent to about seven months of imports at last year's level -- enhance Indonesia's ability to finance necessary food imports. Additionally, the country can sell or barter oil for rice in a good energy market.

order of 800,000 tons -- to cover ~~CONFIDENTIAL~~ shortfalls during 1974. While should remain easier as the world market softens slightly with the Asian and US harvests; unless delivery can be arranged, however, some shortages may occur just prior to Indonesia's May 1974 harvest.

Although the continuing arrival of imports should ease Indonesia's rice problems, some economic pressures will persist. Though by no means approaching the Sukarno standard, Indonesia's inflation -- fueled by rising rice prices -- has been fairly severe this year. For the first nine months of the year, consumer prices showed a 26% increase, compared with 17% for all of 1972 and 4% for all of 1971. Domestic price inflation should moderate during late 1973 and early 1974 but will probably rise again just prior to the May harvest. Early August riots in Bandung, West Java, stemmed largely from deteriorating economic conditions. Following this, residents of East Java were reportedly apprehensive that economic-related problems could provoke similar incidents there.

~~CONFIDENTIAL~~Thousand Tons, Milled

Rice Production (1973)	:	275-300
Rice Production (1972)	:	275
Imports Required (Annual)	:	75-100

Domestic milled rice production has declined steadily from the high of 335,000 tons reached in 1969. Poor weather in several years, combined with military activity that drew labor resources, destroyed fields, and kept large segments of the population on the move, were largely to blame. A small local surplus is produced in southern Laos and is marketed across the border in Thailand because transport difficulties related to insecurity preclude using it to reduce import demand in the major deficit area of Vientiane.

Laos relies heavily on Thailand for the bulk of its grain imports. Persistent market shortages have occurred this year, however, because of shortfalls in the 1972 Thai harvest and Bangkok's reluctance to authorize rice exports. Government-to-government contracts with Thailand signed in September will enable some 370,000 refugees and 75,000 military personnel, almost entirely dependent on rice distributed largely through US assistance, to be supplied until the Lao harvest in December. Imports will still be required throughout 1974, even though Laos has returned to peace for the first time in over a decade and production in its

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... and such a small share of Thai production and
... however, that -- if Thailand's situation improves
... as expected -- few supply problems are envisaged.

The combination of reduced imports and higher world prices has resulted in a doubling of domestic rice prices during the past year, with little rice available in the marketplace at official prices. Despite commodity shortages and inflation of some 30%-40% annually caused largely by the government's chronic deficit-spending, however, the populace is war-weary and relatively apathetic; and rice problems are unlikely to affect even the fragile peace that exists there. Moreover, there are no indications of impending large-scale cutbacks in the multinational, donor-supplied Foreign Exchange Operations Fund, the mechanism through which Laos finances the bulk of its imports.

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Rice Production (1973)	:	1,100
Rice Production (1972)	:	1,000
Imports Required (1971)	:	125-150

With the exception of 1970/71, when flooding damaged some of the rice crop, Malaysia has been steadily progressing toward a goal of 90% rice self-sufficiency. Most of the production increases have come about from a twofold increase over the past five years of the total area under double-cropping. Increasing use has also been made of high-yield rice varieties, some domestically developed.

Malaysian rice imports are relatively small, but the general shortage of world grains has forced the government for the first time to actively participate in rice deals totaling 125,000 tons with China and Thailand -- traditional suppliers through private dealers. This was motivated by a run on domestic supplies in May and June because of consumer and retailer hoarding after Thailand and Burma announced rice export bans. Private dealers imported some 62,000 tons of rice during the first half of 1973; but, since the government's intervention in the market, these dealers have dropped out because they cannot afford to sell at the controlled retail prices.

Among the importing countries of Southeast Asia, Malaysia is relatively well-prepared to cope with rice requirements. The government maintains strict trade surveillance, requires

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extensive stockpiling of in-country rice movement, and usually maintains reserve stocks amounting to 15% of production. Moreover, Malaysia harvests rice almost year-round, which minimizes the severity of any seasonal shortages. Over the longer haul, it has the know-how and irrigation infrastructure for growing two rice crops a year and the short-term, high-yield hybrids to further boost production.

The high prices of rice imports that Malaysia will need to supplement its domestic production will contribute to an inflation* already spurred by booming demand for its primary exports and a surge in domestic consumption, but the impact is likely to be modest. Well-organized government rice marketing programs will minimize the price effect and, given the present position of near self-sufficiency in rice and increasing prosperity on the domestic front, the outlook for political stability seems good.

Similarly, the effect on Malaysia's foreign exchange reserves position created by supplementary rice imports should be minimal. Due largely to the earnings from its export of primary products, the nation's trade surplus recorded a 300% increase during the first five months of 1973 over the corresponding period in 1972 to \$106 million, contributing to an already favorable international reserve

* Consumer prices increased at an annual rate of over 13% during the first five months of the year.

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for the remainder of the year, and even sizable rice imports
could be unlikely to make large inroads into the nation's
reserve holdings.

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Rice Production (1973/74)	:	3,400 - 3,500
Rice Production (1972/73)	:	3,000
Imports Required (1974)	:	400

Seven years after the birth of the "Green Revolution" in the Philippines, two successively poor rice crops in 1971/72 and 1972/73 resulted in critical domestic rice shortages. Central Luzon, which produces about 25% of the Philippines' rice crop, was seriously affected by tungro disease in the 1971/72 season, and total output dropped by almost 5%. The next year's crop in the same area was hit by disastrous floods, while other areas experienced drought; production nationwide dropped over 9%. The situation was made worse by conspicuous decline in some of the elements that had contributed to sizable yield increases in the late 1960s. Specifically, gains from high-yield rice varieties could not be sustained over the longer term without extensive and expensive improvements in irrigation, fertilization, and weed control; Manila reduced its production promotion efforts; and the available funds for rural credit began to contract in 1970.

Despite the Philippines' relatively good foreign exchange position* and a world wide purchasing effort, tight

* The tonnage of rice needed to cover the current shortfall would cost about \$120-\$130 million. Current foreign exchange reserves are about \$800 million, or 7 months' normal imports of all goods.

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normal consumption with imports. Consequently, domestic stocks, down from some 456,000 tons during the crop year 1972/73 to only 256,000 tons, have continued to decline. An import target of 600,000 tons was set for calendar year 1973; however, only 325,000 tons were secured, and pressures on government stocks have increased considerably as the year wore on.

The government took a number of measures to lessen the effect of the shortage on consumers, including control over all rice and corn stocks in the country. A bumper crop in 1973 enabled the government partially to substitute both imported and domestic corn for rice. This initially met with considerable consumer resistance, but now seems to have been grudgingly accepted. The ceiling price on wheat flour, which had been below the world price, was raised to encourage heretofore unprofitable flour imports for noodle and bread production. The support price for paddy was increased by 6% to encourage production, and retail rice prices were increased by 17% to draw out retail stocks. Despite publicized penalties, however, these controlled prices are rarely kept. The market price for the rice-corn mix, for example, has been three times the ceiling price. After several instances of rice being unavailable on Manila markets in August, rationing of the rice-corn mix was instituted.

The situation remains tight, but the prospect of critical food shortages has been considerably lessened with the advent of the 1973/74 harvest now taking place. This crop, however, may be smaller than anticipated because of possible typhoon damage earlier in the year, and the Philippines will likely have to import 400,000 tons of rice in calendar year 1974. The rice should begin arriving in mid-April if it is to cover the critical period until the next crop becomes available in October 1974.

Problems of inflation, spurred by the rice problem and likely to be exacerbated by other commodity shortages, also remain troublesome. Food shortages and a record budget deficit have put a severe strain on prices this year. Wholesale prices were up 25% overall in the first 7 months of 1973 compared to 10% for all of 1972. Stopgap measures seem to have had some success in holding down retail price increases in the short-term, but an easing of inflationary pressure does not appear in prospect. Even with improvement in the rice situation, the Philippines now faces severe cutbacks in crude oil supplies that will aggravate the price situation. Should the rice situation again deteriorate, this combined with a severe shortage of fuels could lead to greater political unrest.

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in return the Philippines to food self-sufficiency. This could be accomplished with superior weather, but any sustained long-term growth will require an extensive government program to increase irrigation and fertilization and maximize the yields from newer rice strains. Primarily, credit availability must be improved through a rational lending program insuring adequate funds for input purchases with interest rates and sanctions that encourage repayment.* In addition, the program to substitute corn and wheat consumption will have to be encouraged even when rice is not in short supply.

* One of the major problems with the highly-publicized land reform program, for example, is that small farmers were cut off from their major source of credit, the landlord, and the government did not step in with alternative funds.

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~~CONFIDENTIAL~~ Thousand Tons, Million

Rice Production (1973/74)	:	3,700 - 3,900
Rice Production (1972/73)	:	3,500
Imports Required (1974)	:	450

After three years of production increases, greater military activity and poor weather resulted in an estimated 5% decline in the 1972/73 rice harvest. Continued poor weather in some areas, uncertainty as to market access, and much higher fertilizer and other input prices apparently held production down below potential for the 1973/74 crop as well, but record harvests totalling over 6 million tons are still possible.

Although the rice crop has still not grown enough to eliminate imports, a much higher than expected level of shipments from the Delta from both current production and privately-held stocks has eased considerably the fears of a severe shortage later this year. During September, about 65,000 tons of rice apparently were moved out of the Delta into government stocks. This was one of the highest monthly totals in years and by far the highest for September, when Delta stocks are traditionally low prior to the November-January harvest. The major reason for the increased shipments was the government's heavy pressure on Delta merchants to reduce inventories, suppress speculation, minimize

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transported rice to Saigon.

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Prior to the announcement of high September shipments and government stocks, the Thieu government was privately projecting that stocks for supplying rice-deficit areas would be depleted by December of this year unless early PL-480 imports or increased Delta deliveries were achieved. Moreover, a black market for rice -- the first in years -- had sprung

* Much as the Saigon government's rice situation has worsened this year, so too have the VC/NVA been upset in their efforts to meet immediate requirements. The Communists have a large demand for rice to feed military personnel and civilians in the occupied or controlled areas. Most of the civilians and some of the military requirements are, however, met from sources other than GVN areas, such as local cultivation, use of accumulated stocks, and imports from North Vietnam. Moreover, the civilians in VC/NVA areas are probably expected to meet a large share of their food requirements themselves, and are not properly a burden on the Communist government's food supply system. Although data for total rice requirements in Communist areas are necessarily based on crude estimates, it appears that these areas need to "import" less than 100,000 tons.

Much of this will probably flow in simple individual purchases by civilians who visit GVN markets or in the traditional "tax" collections from farmers in contested areas. For the remainder, the VC/NVA will need to augment rice flows from North Vietnam or move more aggressively into GVN markets. Sufficient rice could be diverted from North Vietnam to South Vietnam if need be without seriously upsetting the North's own rice supply situation; this move, moreover, would be facilitated by new roads being constructed in Laos and South Vietnam.

Seeking to meet their own requirements and, where possible, to exploit GVN rice problems, the Communists have intensified their efforts to secure rice in South Vietnam. This includes such elements as transport and marketing disruptions, stock seizures, and confiscation of the upcoming harvest. Short of large scale military operations in the Delta, however, these measures are unlikely to disrupt harvesting over a broad enough area at any one time to cause a critical loss of South Vietnamese production.

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in Saigon, which sold for about 50% above the official price, which in turn was some 60% higher than at the beginning of the year. In response to these developments, the government on 22 September initiated direct rationing for rice. Rice sales from official outlets in the Saigon metropolitan area were limited to 20 kilograms per family each month, or roughly one-third of average requirements. The black market still flourished, however, and accounted for most rice sales in Saigon. With the early October improvement in stocks attendant on increased Delta deliveries, a decision was reached on 10 October to increase the monthly ration from government-supplied outlets to 40 kilograms per family, and this ration was raised to 50 kilograms a week later.

The prospects for the government's maintaining adequate rice stocks through the remainder of the year are now much improved. Preliminary reporting indicates that Delta deliveries in October also could be substantially greater than anticipated earlier. Thus, it now appears that the end-of-November government stock position will be at least one month's normal consumption.

Even assuming the arrival of as much as 65,000 tons of US PL-460 rice in December, the rice situation will

...remain tight for some time. The rice black market continues to co-exist with government sales from official outlets. The increased government ration in Saigon and the expansion in recent weeks of government sales at subsidized prices throughout the country have caused black market prices to recede only slightly, and the price of rice remains an important economic and political issue.* Moreover, heavy November rains in the northern section of the country have damaged that area's rice crop and driven out several thousand farm people who will now depend in part on government supplies. Finally, nationwide rice inventories are currently very low; rebuilding them will require some 450,000 tons of PL-480 shipments in 1974 -- costing the government \$20-\$25 million in freight costs -- as well as a good domestic harvest.

The longer-term consequences of this year's heavier government intervention in the rice market are still unclear. The military commanders most responsible for the increased Delta shipments have already announced proposals for a

* Reflecting its major role in personal spending, rice is by far the largest item in Saigon's retail price index, and the doubling of retail rice prices recorded since the start of this year is the major factor in the index's overall increase of 50%. At today's retail prices and at an average per-capita consumption rate of 155 kilograms per year, rice would cost the equivalent of \$48 per person year, about one-third of estimated per-capita income. Substitution of less expensive food and subsidized government rice sales, particularly to the military and civil service and their families, ease both the personal burdens and the inflationary impact, but these remain considerable.

... of the private rice trade. If the government increases its already strong controls over distribution and price levels -- and this now appears more likely -- farmers' production incentives could be adversely affected.

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Other long-term agricultural growth problems, besides security and the weather, include shortages of farm labor because of increasing urbanization; the highly capital-intensive nature of South Vietnamese agriculture, which may slow productivity growth as inputs inevitably become more expensive; a typical shortage of adequate credit; lack of a well-planned crop diversification program; and, except for highway transportation, a weak internal marketing system.

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World Outlook for the Current Crop Year

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This year's rice crop in Southeast Asia is as good as foreseen. World rice production could reach or even exceed the record 1971/72 crop of 300 million tons of paddy. Considering scattered late reports of crop damage, this may be unduly optimistic as a pre-harvest estimate. In any case, prices should soften somewhat as newly-harvested rice hits the market near the end of 1973, but will continue higher than those of 1972. A crop of this magnitude would also stop further drawdowns on present low rice stocks, but will not allow for the rebuilding of rice reserves.

Irrespective of production levels, import demand will continue to be high throughout 1974, and some shortages may occur especially in May and June. Moreover, domestic demand will have increased because of population growth and steadily increasing per-capita rice consumption. Several countries -- Indonesia and the Philippines, in particular -- have expressed a desire to build up large stock levels, but this would be impossible this year.

The US plays a major role in world rice trade, accounting for more than a quarter of the rice entering world markets since 1967. Production for 1973/74 is estimated at 4.3 million tons of paddy, up 12% over last season. Only a slight increase over last year's exports of 1.8 million tons is

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achieved, however, because the 1973 level was achieved by drawing down domestic stocks to the lowest level in a decade. In particular, only some 600,000 tons of rice are expected to be available for export on concessional terms (compared to 1.3 million tons from the 1971/72 crop and 940,000 tons from last year's crop), and these will be limited to South Vietnam, Cambodia, and -- possibly -- Indonesia. Moreover, as much as 300,000 tons of next year's PL-480 availabilities may have already been committed before the end of this year.

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7. Worldwide Rice Supply in 1974/75

As common stated recently in 1972, worldwide rice production is at the mercy of the weather. Increases in acreage and crop development efforts -- especially more widespread use of high-yield rice varieties -- are important adjuncts and properly utilized can contribute to favorable long-term growth trends. Given the present state of technology, however impressive growth can just as impressively be set back by a whimsical typhoon.

Assuming a near-record 1973/74 crop, it will take another record crop in 1974/75 to fully recover from the poor production of 1972/73. With two bumper crops back to back, there may be enough rice available to replenish stocks and possibly afford an opportunity to purchase additional buffer reserves.

The US will continue to be a major rice supplier in 1974/75, but measures are being taken to guard against a collapse of the international market. Because of the extremely high rice prices this season, competitive market forces alone would have stimulated an estimated 250,000 hectare increase in US rice plantings in 1974/75. This could have led to a large surplus in US production and a depression of prices at the farm. Consequently the USDA

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... program for next year calls for a reduction in the ... under which guaranteed price ... (at 500 of parity) are authorized from some 890,000 hectares to about 800,000 hectares; plantings in excess of this figure will receive no price supports, and new producers will not be eligible for farm loans. Alternatively, however, for the first time since 1954 rice marketing quotas have been lifted. This means that for next year's crop, farmers will not be penalized for production in excess of established quotas.

The net effect of the crop program will likely be to encourage increased plantings and yields through the removal of penalties, even though incomes may be jeopardized by the reduction in price-supported acreage. US production is projected to be some 4 million tons milled, a 38% increase over 1973/74. While unlimited export demand cannot be assumed to continue throughout 1974/75, it should nonetheless be high based on the difficult market experiences of this past year. Of course, any serious drop in Asian production would intensify pressures on US supplies.

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Annex A.

Rice Situation in North Vietnam

		<u>Thousand Tons, Million</u>
Rice Production (1973)	:	2,700 - 3,000
Rice Production (1972)	:	3,000 - 3,100
Imports Required (July 1973 - June 1974)	:	600 - 800

(Although global and regional data in the text of this report include North Vietnam, its rice situation over the next few years differs in some substantial details from that of the rest of Southeast Asia. North Vietnam probably will not receive any significant quantity of US PL-480 during this fiscal year. Moreover, it has traditionally met its import requirements through shipments from the Communist countries. Internally, North Vietnam's rice problems have tended to be masked by a rather rigid system of state procurement and food rationing, and this distinguishes its economic pressures -- at least in detail -- from those of non-Communist countries faced with meeting stabilization goals.)

North Vietnam should show a mediocre performance in rice production this year. The spring crop, which accounts for about one-third of production, was reasonably good. Several major growing areas suffered from a combination of premature planting

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... various diseases, and adverse weather, ... probably amounted to about 1.2 million tons of paddy. Official press statements claim that the crop was less than last year's, but the third best in over a decade.

There is little direct evidence on the 1973 autumn crop, which is harvested during October and November. This is the first autumn crop in recent years to benefit from peaceful conditions, but the harvest is unlikely to be any better than last year's estimated 2.6-2.8 million tons of paddy. Drought at the beginning of the autumn growing season and heavy rain during transplanting destroyed some seedlings and waterlogged paddy fields. North Vietnam has been affected by six tropical cyclones this rainy season, compared with three last year, and flooding was reported in several areas. Although this year's flooding did not approach the disaster of 1971*, it probably limited output somewhat.

North Vietnam has little difficulty meeting its food needs through imports. North Vietnam normally imports 400,000 - 600,000 tons annually of rice, wheat flour, and corn, almost entirely from China and the USSR.** Imports this year, however,

* Destructive floods in the late summer of 1971 dealt agriculture a particularly severe setback. Some 450,000 hectares of land were flooded sufficiently to destroy the entire rice crop, and perhaps half the crop was destroyed on another 200,000 hectares.

** China probably considers North Vietnam its first priority; hence, exports to North Vietnam necessarily limit those that can be sold to the Free World.

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Since 1975, Hanoi has been running at an annual rate of 200,000 tons. Since 1975 has been no reported change in the average per-capita grain ration of 1.3-1.4 kilograms a month, this suggests that considerable grain is being used to replace stocks severely depleted during the war and to build a contingency against future natural -- and military -- emergencies.

Hanoi has made little progress in achieving rice self-sufficiency, a goal of the post-war reconstruction and development effort. Indeed, even at a robust annual growth rate of 5%, such a target would be some 10 years off. With the primitive prevailing technology, the crop is still quite sensitive to inundation, water-logging, drought, insects, and diseases. By Hanoi's own admission, the water control network is poor. Inadequate irrigation and low levels of fertilizer and pesticide applications limit the grains obtained from the high-yield rice varieties that are planted on over two-thirds of the spring crop area. Corn is being emphasized as a substitute for rice and as feed for animals, but little is being done to increase its production. Moreover, the cooperative system works against large increases in agricultural output. It stifles managerial initiative, and there is little incentive for the farmer to increase his own productivity. Shortcomings in the cooperative system have been recognized by government leaders, and some reforms for increasing incentives have been suggested.

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Based on experience of the past decade, the prospect of serious political or economic difficulties ensuing from shortages in North Vietnam appear remote. The government's institutional framework insures pervasive control over distribution of food supplies. Food staples -- grain and meat -- are evenly rationed in modest amounts, and prices for these rations are fixed. The only area of competitive bidding for supplies is the government-monitored free market, which is limited largely to vegetables and handicrafts. China and the USSR have covered food deficits for years, and this will continue to be the case in 1973-74. Under these circumstances, the country seems destined to enjoy a relative insulation from world food problems.

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